

**MINUTES OF THE REGULAR MEETING OF THE  
ARIZONA STATE RETIREMENT SYSTEM BOARD**

**HELD ON  
July 16, 2004  
9:30 a.m., MST**

The Arizona State Retirement System (ASRS) Board met at Northern Arizona University, Facility Services Conference Room A, 575 Pine Knoll Drive, Flagstaff, Arizona 86011 Dr. Keith Meredith, Chairperson of the ASRS Board, called the meeting to order at 9:30 a.m., MST.

The meeting was teleconferenced to the ASRS office at 3300 N. Central Avenue, Phoenix, Arizona and 7660 E. Broadway, Tucson, Arizona 85710.

**1. Call to Order; Roll Call; Opening Remarks**

Present: Dr. Keith Meredith, Chairperson  
Mr. Karl Polen  
Mr. Jaime Gutierrez  
Ms. Anne Mariucci (Via teleconference)  
Mr. Michael Townsend  
Mr. Lawrence Trachtenberg  
Mr. Steven Zeman

Absent: Mr. Jim Bruner  
Ms. Charlotte Borchert

A quorum was present for the purpose of conducting business.

**2. Approval of Consent Agenda**

**Motion:** Mr. Michael Townsend moved to approve Refunds, Death Benefits, Retirements, and System Transfers,

*And*

Approve the Application & Agreements with the Following employer:

- Eloy Fire District

*And*

Approve the minutes of the June 18, 2004, Regular Board meeting of the ASRS Board,

*And*

Approve the Recommended Order on the Appeal of Heidi Warner,

***And***

Approve the Notices of Rulemaking Docket Opening for employer membership and service purchase.

Mr. Steven Zeman seconded the motion.

By a vote of 6 in favor, 0 opposed, 0 abstentions, and 3 excused, the motion was approved.

*Mr. Karl Polen arrived at the meeting at 9:40 a.m.*

### **3. Presentation, Discussion and Appropriate Action Regarding an Overview, Status Update, and Key Initiatives of the ASRS**

Mr. Paul Matson, Director, provided an overview and status update on investments, compliance, contribution rates, and service purchase payroll deduction agreements. Additionally, Mr. Matson touched on the following key initiatives:

- Agency Governance
- Strategic Analysis
- Securities Litigation Infrastructure
- Health Insurance Issues
- Information Technology Plans
- Budget Update
- Rules & Policy Review
- Equity & Efficiency Analysis
- Senior Staff Recruitments
- Legislative Update

### **4. Presentation, Discussion and Appropriate Action Regarding the Notice of Final Rulemaking for R2-8-123, Actuarial Assumptions and Actuarial Value of Assets, and R2-8-126, Calculating Benefits**

Ms. Nancy Johnson, Rules Coordinator, stated that the ASRS Board approved the new actuarial assumptions for the plan members at its November 21, 2003 Board meeting. In January, the ASRS filed a Notice of Rulemaking Docket Opening for R2-8-123 and R2-8-126 with the Secretary of State. The Attorney General's Office approved the Emergency Rule Making for R2-8-123 and R2-8-126, and filed it with the Secretary of State on June 3, 2004. The Proposed Rule Making was published in the Arizona Administrative Register May 7, 2004, and an Oral Proceeding held on June 7, 2004. No interested persons attended the oral proceeding and the ASRS received no comments on the rules. Therefore, the Final Rule Making has no changes from the Proposed Rule Making.

ASRS staff proposes that the Board approve the Notice of Final Rule Making.

**Motion:** Mr. Michael Townsend moved to approve the Notice of Final Rule Making for R2-8-123, Actuarial Assumptions and Actuarial Value of Assets, and R2-8-126, Calculating Benefits.

Mr. Karl Polen seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, and 2 excused, the motion was approved.

## **5. Presentation, Discussion and Appropriate Action Regarding the ASRS Real Estate Program**

Mr. Gary R. Dokes, ASRS Chief Investment Officer; Mr. Cesar Porte, ASRS Real Estate Portfolio Analyst; Mr. Michael Humphrey, Principal, Courtland Partners; and Mr. David Linn, Senior Consultant, Courtland Partners presented on this agenda item.

At its August 15, 2003 Board meeting, the ASRS Board approved an allocation of 6% +/-2% to institutional real estate as part of the ASRS' new asset allocation policy. On November 21, 2003, The ASRS Board approved the hiring of Courtland Partners as ASRS' real estate consultant. In February 2004, a real estate portfolio manager was hired in the Investment Management Division (IMD). Over the past four months, the IMD and Courtland Partners have developed an ASRS Real Estate Program.

Upon adoption of the ASRS Real Estate Program, a Real Estate Committee will be created and will implement the program which includes the search and hiring of legal counsel and managers. Any recommended changes in this program such as portfolio structure, decision-making process, and strategic and/or tactical allocation will require Board approval.

The Investment Review Committee (IRC) recommends that the ASRS Board adopt the ASRS Real Estate Program.

**Motion:** Mr. Karl Polen moved to approve the IRC recommendation to adopt the proposed ASRS Real Estate Program.

Mr. Steven Zeman seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, and 2 excused, the motion was approved.

## **6. Presentation, Discussion and Appropriate Action Regarding the ASRS Vision & Values**

At the June 18, 2004 Board meeting, a new Vision and Values statement for the ASRS was presented by Mr. Matson. After the discussion, there was support for the Vision and Values statement but several recommendations were made to simplify the language. Mr. Matson reviewed the language while taking into consideration all comments made at the meeting and during additional follow-up contact with Board trustees. Below is the revised Vision and Values statement:

## **Vision**

For the benefit of our members, the Arizona State Retirement System will be a leading state benefit plan administrator in the areas of:

- Core Member Services
- Funded Status
- Investment Performance
- Operational Effectiveness

This will be accomplished while keeping program benefits and associated costs relatively aligned and maintaining actuarial and fiscal integrity.

## **Values**

Our organizational culture will be based upon the following Values:

- Service:*** A commitment to service excellence will permeate the organization.
- Professionalism:*** A highly capable workforce will promote a professional and respectful environment and lead the organization.
- Improvement:*** A climate of continuous quality improvement and enhanced efficiencies will drive the organization.
- Diversity:*** Engagement of diversity by the appreciation, recognition, and support for all people will propel the agency to ever greater achievement.
- Results:*** A results-oriented approach to operations will energize the organization.

**Motion:** Mr. Jaime Gutierrez moved to approve the ASRS Vision & Values statement with the amendments as discussed.

Mr. Michael Townsend seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, and 2 excused, the motion was approved.

## **7. Director's Report**

Mr. Matson briefly commented on the Compliance Section of the Director's Report for the benefit of the members.

Mr. Matson also brought to the attention of the Board the retirement of two ASRS employees, Mr. Ray Fuller and Ms. Victress Jenkins. He stated that these two employees should be commended for all of their hard work as they are a part of the ASRS and have contributed to what the ASRS is today. They will be missed.

## **8. Presentation and Discussion Regarding Board Committee Updates**

Dr. Meredith stated that the External Affairs Review Committee will be reviewing the ASRS appeals process. Revisions to this process will be presented at the next ASRS Board meeting.

## **9. Board Requests for Agenda Items**

None.

## **10. Call to the Public**

Mr. Dan Julian, Retiree from Northern Arizona University, requested to address the ASRS Board. Mr. Julian stated he was concerned about when the enhanced rural insurance subsidy ends on June 30, 2005, for retirees in the rural areas because the premiums continue to increase.

## **11. Presentation, Discussion and Appropriate Action Regarding an ASRS Investment Manager**

**Motion:** Mr. Lawrence Trachtenberg moved that the ASRS Board convene to executive session at 11:05 a.m.

Mr. Steven Zeman seconded the motion.

The ASRS Board reconvened to Regular session at 11:15 a.m.

**Motion:** Mr. Lawrence Trachtenberg moved to approve the termination of Columbia as the ASRS U.S. Equity small cap growth manager;

***And***

Moved to approve BGI as the interim ASRS small cap growth index manager to transition the Columbia portfolio to a passive portfolio and manage assets until a replacement active small cap growth manager is approved by the Board;

***And***

Moved to authorize IMD/Mercer to conduct a small cap manager search and recommend to the IRC/Board a replacement active small cap growth manager.

Mr. Karl Polen seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, and 2 excused, the motion was approved.

**12. The next ASRS Board meeting is scheduled for Friday, August 20, 2004, at 8:30 a.m., at 3300 N. Central Avenue, 10<sup>th</sup> Floor Board room, Phoenix, Arizona 85012.**

Dr. Meredith called a recess of the ASRS Board meeting at 11:20 a.m.

The Board reconvened at 12:40 p.m. The following Board Trustees were present: Dr. Keith Meredith, Mr. Karl Polen, Mr. Jaime Gutierrez, Ms. Anne Mariucci (via teleconference), Mr. Michael Townsend, Mr. Lawrence Trachtenberg, Mr. Steven Zeman.

**13. Presentation, Discussion and Appropriate Action Regarding Strategic Analysis on the Following Topics**

The Board commenced strategic analysis and review of topics that will affect the ASRS for the next five to ten years.

**Actuarial Status**

Mr. Matson gave background on the rising contribution rates, funded status and plan design. Mr. Matson explained that the factors affecting the actuarial status are investments, benefits, methods of benefit implementation, and methods of assumptions.

ASRS staff indicated that they will move forward with further analysis.

**Health Insurance**

Dr. Meredith introduced the Health Care issue stating that health care costs will continue to increase and the ASRS must continue to work on ways of reducing these costs for its members. Possible methods of doing so are to have pre-Medicare eligible retirees enroll in their employer's plan; to educate members on the causes of increased costs and what they can do to keep the costs stable; to investigate becoming a self-funded and/or self-managed health care plan; and to find ways to expand the enrollment and spread the risk by putting all pre age 65 retirees into a common pool or possibly blending active members with retired members.

Currently, the ASRS is assisting the Legislature with a study on retiree health insurance. The study will review the feasibility and cost impact of allowing all retired members of the state's retirement systems to participate in the state employee health insurance program that is administered by the Department of Administration.

**The Hybrid Defined Contribution System**

Mr. Richard Stephenson, Deputy Director, External Affairs explained the background of the "System." The System was created in 1953 as a defined contribution plan. In 1971 membership was closed and the "Plan," a defined benefit plan was created. System members were given the opportunity to switch to the Plan and 80% chose to do so. Currently there are 2,194 System members, 1,891 are retired and 303 are non-retired. Ninety-eight of the non-retired members are actively contributing and there are 205 inactive members whose whereabouts are unknown.

Mr. Charlie Chittenden, the ASRS actuary, has established that with 1,000 members, the System fund will remain balanced. The System should reach 1,000 members in 2015. Once the System

has 200-300 members, it is likely that the benefits will need to be adjusted annually. The System should reach 268 members in 2027, making it difficult to maintain the desired balance of assets to liabilities and benefits will need to be adjusted. At that time, possible solutions may be to transfer all system members to an insurance company, provide a lump-sum settlement, or roll them into the ASRS plan.

Staff and the ASRS actuary will continue to monitor System assets, liabilities, membership, and funded status and provide a detailed annual report to the Board. The report should establish benchmarks to determine when action must be taken.

Board Trustees also gave staff direction to contact the 205 inactive members of the System to ensure they are aware of the benefits they are entitled to.

**Ms. Ann Mariucci was excused from the meeting at 3:00 p.m.**

### **Long Term Care Insurance**

Mr. Zeman explained that at its November 2003, public meeting, the Operations Review Committee recommended that the ASRS staff investigate the administrative and operational implications of offering a voluntary Long Term Care (LTC) insurance product to the ASRS' 200,000 active and 64,000 retired members.

The long term care insurance program would be an employee or retired member driven program (e.g., no premium deduction through pension payroll, and no IT involvement). The marketing of the program would be shared by the ASRS and the successful bidder. The administration of the program would be the responsibility of the vendor.

A request for information (RFI) will be issued for the purpose of obtaining more information on a LTC program.

### **State Requirements for Budget, Personnel, Procurement**

Mr. Anthony Guarino, Deputy Director, Chief Operations Officer, stated that in a Board report on Governance Policy, Mercer Investment Consulting concluded that systems without budget autonomy have experienced operational problems, including poor customer service.

According to Mercer, removing the operating budget from the legislative appropriations process would better enable the Board to accomplish ASRS goals and objectives. Recent experience tends to support Mercer's position.

Regarding Personnel Administration, Mr. Guarino stated that there are no particular problems with the ASRS following the Arizona Department of Administration (ADOA) personnel administration rules. However, adhering to classifications determined for state employees by the ADOA limits the Board's and Director's discretion in classifying and setting salaries for agency personnel. This is an issue for the Board only to the extent that this may impede the Board's ability to recruit and retain qualified staff.

With respect to procurement, there are no current problems. This could change however, as the ADOA is reviewing measures which, if enacted, would place the ASRS procurement officers

under its control. The rationale is that state government would benefit from efficiencies gained from a pool of procurement officers, and its impact on the ASRS is unknown.

There was a consensus that removing the ASRS operating budget from the legislative appropriations process would benefit the ASRS, and staff will recommend it to the External Affairs Review Committee as possible legislation.

### **Trustee Terms**

Mr. Stephenson explained that during the recent Governance Study, it was discussed that the current three-year term might not provide for the greatest continuity in ASRS oversight. Furthermore, it was expressed that longer terms would allow more time for new Board Trustees to become familiar with the issues and activities and therefore be more effective as Trustees.

It appeared that at this time, changing the length of Trustee terms is not a critical issue.

### **Director's Outreach Forum**

Mr. Matson reported that he is considering a forum to allow more direct contact and interaction between members, the Director and others in the agency. Mr. Matson discussed plans for a Director Outreach Forum. The Forums would be scheduled approximately four times a year. In each of the forums the Director would make available other ASRS subject matter experts to respond to questions.

Board Trustees agreed that the Forums would add a lot of value to the membership, and would be most effective if also held in areas such as Yuma and Flagstaff. It was also suggested that rather than holding the Board meetings in areas outside of Phoenix, it may be more cost effective for the ASRS and informative for the members if Director Outreach Forums were held instead.

## **14. Adjournment of the ASRS Board**

Dr. Meredith adjourned the July 16, 2004 Board meeting at 4:00 p.m.

## **ARIZONA STATE RETIREMENT SYSTEM**

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Marina Chaves, Secretary

Date

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Paul Matson, Director

Date